

**USAID/Kyrgyzstan**

**Annual Report**

**FY 2004**

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## Kyrgyzstan

### Performance:

**BACKGROUND:** Kyrgyzstan was the first Central Asian republic to undertake meaningful economic and social reform. It inherited one of the least competitive economies of the former Soviet Union, with relatively few natural resources other than water. While it has good agricultural and tourism potential, it is severely handicapped by protectionist measures and corruption in neighboring countries, both of which impede exports. Internal corruption is also a very serious and growing constraint. The most critical question at this juncture is the struggle between reformist elements within the government and those seeking to resist reform, maintain control of the economy by the ruling oligarchy, and avoid revelation of past corrupt practices in which external debts grew from zero in 1991 to over \$1.9 billion. Intense maneuvering in this regard is taking place in the lead up to the 2005 parliamentary and presidential elections. The President has stated publicly that he will step down in 2005, perhaps signaling a chance for real democratic reform. Calls for him to remain, however, are coming from many sectors, and the current draft elections and political parties' codes (still being debated) are far from meeting international standards.

Freedom House ratings worsened during the year in electoral process (6); independent media (6); governance (6) and constitutional, legislative, and judicial framework (5.5). [Note: 7 is the worst score]. Nevertheless, civil society in Kyrgyzstan, while very donor-dependent, is far more developed and free than in other Central Asian countries. The civil society rating held steady at 4.5. Non-governmental organizations (NGOs), civic organizations, and media are able, at times, to exert positive influences on government policy and legislation. Parliament sometimes provides a check on government authoritarianism. Local governments are increasingly transparent and responsive. Local elections in over 460 villages and cities represented the first direct local elections in Central Asia and resulted in over 40% of the incumbents being ousted. The Constitutional Referendum held in February of 2003, however, was a major setback for democracy in the Kyrgyz Republic; it greatly increased Presidential control and limited both judicial and Parliamentary independence as well as the activities of civil society.

Government data show that, during the first 10 months of 2003, GDP grew by 5.9%, mostly due to recovery of the Kumtor gold mine after a partial closure in 2002. Per capital income grew at 1.5% annual rate. The average monthly salary went up 13.5%, now equivalent to approximately \$40. There was a slight increase in the volume of exports, but imports grew by 25.6%. External debt was \$1.9 billion at the end of the first quarter of 2003, a 7.8% increase over the first quarter of 2002. Tax collections increased by about 14% and inflation was about 2.6% during the first 10 months of 2003. The currency has remained essentially stable against the dollar. Exports suffered from the closure of the Uzbek border, the costs of getting trucks through Kazakhstan, and protectionist measures from such neighbors. Banking deposits increased by 25% which, together with investments by three Kazakh banks, indicates increased confidence in the system. Total foreign currency reserves grew to approximately \$180 million.

Limited access to trade routes, a heavy burden of external debt (\$1.9 billion), a weak banking sector, as well as internal corruption at all levels, threaten economic and political reform and limit growth. Poverty and limited opportunities particularly jeopardize stability in the south, where isolation, difficult borders, lack of investment, and ethnic differences are problems.

**U.S INTERESTS AND GOALS:** Kyrgyzstan's support of the coalition airbase near Bishkek and associated over-flight rights were essential to allied successes in Afghanistan and Iraq, and Kyrgyzstan continues to be a strong strategic partner of the United States and others. Because regional stability is a key foreign policy goal, the potential for the messages from extremist groups (e.g., IMU and Hizb-ut-Tahrir) to take hold among the country's vulnerable populations and those dissatisfied with government is

also of concern. Our economic and financial programs benefit the poor, unemployed, and small/medium enterprises (SMEs). Health, education, and democracy benefit all.

**DONOR RELATIONS:** Almost all major multinational donors are active in Kyrgyzstan, together with many important bilateral donors such as the European Union, British, Germans, Swiss, and Japanese. The largest donors are the Asian Development Bank, the International Monetary Fund, and the World Bank. Also important are the European Bank for Reconstruction and Development, the International Organization for Migration, the Islamic Development Bank, the Aga Kahn Foundation, and the Open Society Institute. USAID coordinates with all regularly, working in particular with the World Bank and the United Nations. The World Bank leads the donor coordination efforts in the country and maintains an active database of projects and programs.

**CHALLENGES:** USAID faces an increasing challenge to maintain the direction of democratic reforms, at least at the national level. The flawed constitutional referendum at the beginning of this year was a major setback for democratic institutions in the country in general and for Parliament in particular. Encouraging a peaceful, democratic transfer of power in 2005 is now the primary challenge.

The economy is holding its ground, but still faces serious difficulties. The budget, together with donor funding, is not adequate to address all critical problems. The banking sector has shown some improvement. In other areas, there is often a lack of commitment to follow through with reform recommendations. Reform of the energy sector has yet to occur, which means continued sizeable losses to the state budget through unsustainable subsidies. Trade barriers, such as the border closure with Uzbekistan, protectionist measures from Kazakhstan, and corruption, both internal and in neighboring countries, continue to be formidable. Many lucrative businesses and investment projects have been monopolized by a small group of politically well-connected entrepreneurs. A maze of uncoded "fees" continues to constrain free enterprise.

In the health sector, reliable statistics are badly outdated, with the last full-scale demographic health survey conducted in 1997. Anecdotal evidence is that the situation has deteriorated. Tuberculosis and HIV/AIDS are growing problems. The biggest challenges in health are now low budget allocations and allowing the health sector to keep savings generated through reforms, instead of losing a corresponding amount from the normal (insufficient) budget allocations from the Ministry of Finance.

With the demise of the Soviet Union, Kyrgyzstan, like other newly independent states, suffered a substantial deterioration of the once-strong education sector. Schools lack resources to maintain their buildings and pay staff salaries. Extremely low salaries of teachers provide a disincentive for the younger generation to pursue careers in education, as well as for qualified teachers to remain in the profession, resulting in a lack of teachers, particularly in rural areas. A high percentage of teachers will retire in the next few years; finding replacements will be a major problem.

#### KEY ACHIEVEMENTS:

**IMPROVED ENVIRONMENT FOR SMALL AND MEDIUM ENTERPRISES:** An index of benchmarks on which SMEs are surveyed on issues such as access to training, credit conditions, and government compliance with commercial laws, showed that Kyrgyzstan made modest progress in improving the business environment. Entrepreneurs reported greater access to credit and better credit terms. Work to improve tax administration and state budgeting practices yielded significant results, such as increased tax revenues by more than 14%. As a result of USAID assistance, the Budget Committee now holds quarterly public hearings and publishes the budget online, while the Tax Inspectorate regularly compiles decisions on taxpayer inquiries and makes them available to staff. A new law on technical regulations was drafted which, when approved, will modernize quality standards regulation and reduce the tremendous costs businesses bear in complying with outmoded mandatory standards. A commercial arbitration law was passed. If it is well implemented, it will allow for quicker resolution of disputes and help insulate litigants from corruption and delays in the court system. A new property tax was introduced that will provide local governments with a source of their own revenue and help finance services and infrastructure for local enterprises.

**STRENGTHENED DEMOCRATIC CULTURE AND INSTITUTIONS:** Despite the serious challenges noted above, USAID's efforts to promote democracy have made significant achievements in certain areas. In September 2003, a new law on the financing of local government, drafted with significant input from USAID, was adopted. When effective in January 2005, it will substantially change the centralized system of public finance in Kyrgyzstan and give local self-governments far more authority to determine their own expenditure plans. USAID also met its target regarding municipalities using good management techniques. In the civil society area, the USAID-funded network of NGO resource centers, now numbering 11, was registered during 2003. The NGOs we support undertook a large advocacy campaign in 2003 to allow grants and humanitarian aid to become tax-exempt, conducting 14 roundtables in all provinces of Kyrgyzstan with participation of 350 people from NGOs, mass media, and state institutions. In March 2003, the bill amending the Tax Code was signed by the President and became effective, a major success for civil society generally and for our programs.

**IMPROVED MANAGEMENT OF NATURAL RESOURCES:** A new USAID activity is targeted at identifying the sources of electrical losses in the extensive Kyrgyz electrical grid. Though still in progress, the project is already having an impact. Specifically, the Bishkek distribution company Severelektro has gone beyond the metering improvements provided by the project to upgrade the network in the project area with new poles and wires and has indicated that it wants to use the area as a model on meter reading, billing, and collection. The World Bank has confirmed that it has committed a \$5 million dollar loan to the four distribution companies to mount similar loss reduction pilot projects, following USAID's model.

**INCREASED ACCESS TO PRIMARY HEALTH CARE:** In 2003, USAID overcame opposition to health reform, with a strong expression of support from the President, policymakers, and other stakeholders. Kyrgyzstanis increasingly sought outpatient care from primary health care (PHC) clinics rather than from specialty polyclinics. Nationwide, PHC's outpatient share increased from 53.3% last year to 58.2% (56% target). In 2003, two of five proposed laws (supported by USAID) passed, including the "single-payer" law, which established the Health Insurance Fund as the purchaser for all health services nationwide. These laws will help ensure sustainability of the reforms. USAID efforts also helped the Kyrgyz Republic receive approval for participation in the Global Fund for AIDS, Tuberculosis, and Malaria to the tune of approximately \$19 million.

**EDUCATION:** Our work in primary/secondary education has only begun, but the National Scholarship Testing Initiative, supported by USAID for the second time in 2003, allowed for transparent and fair distribution of state grants for undergraduate study. More than 35,000 applicants competed for over 5,000 scholarships, and 86% of those who received the grants were outside of the capital city area.

**CONFLICT VULNERABILITY:** Kyrgyzstan does not appear to be sliding into open conflict, and conflict has not impeded program implementation. By the close of FY 2003, USAID was working in 27 sites, primarily Ferghana Valley border communities, which have identified sources of local tension. The border closure with Uzbekistan, and extremist elements which prey on the unemployed, are the primary sources of conflict.

**GENDER:** USAID's program addressed gender disparities in a variety of ways. Gender sensitive USAID funding is enabling women's shelters to provide counseling, job training, and accommodation to victims of domestic abuse and self-immolation. FY 2003 saw the launch of a new grant to fight trafficking in persons, which will primarily benefit women. In FY 2004, more attention will be focused on the issue of bride kidnapping.

**TRADE CAPACITY BUILDING:** USAID supports trade capacity-building in Kyrgyzstan through accounting reform and regional trade promotion. In June 2003, the Government of Kyrgyzstan established a new Inter-Agency Commission on WTO Compliance. USAID experts helped draft resolutions, accepted by government, that provide more detail than previous resolutions to ensure greater WTO compliance and improved trade policies.

**Country Close and Graduation:**

## Results Framework

### **116-0110 Privatization**

### **116-0120 Increased Soundness of Tax and Budget Policies and Administration**

### **116-0130 Increased Soundness of Tax and Budget Policies and Administration**

### **116-0131 Improved Environment for the Growth of Small and Medium Enterprises**

#### **SO Level Indicator(s):**

A Business Environment Index

**IR 1.3.1** Increased Opportunities to Acquire Business Information, Knowledge, and Skills

**IR 1.3.2** More Responsive Financial Institutions, Instruments, and Markets

**IR 1.3.3** Increased Implementation of Laws and Regulations

### **116-014 A More Competitive and Market Responsive Private Financial Sector**

### **116-0150 Energy**

### **116-0160 Environmental Management**

### **116-0161 Improved Management of Critical Natural Resources, Including Energy**

#### **SO Level Indicator(s):**

Number of Demonstration Models Replicated in the Central Asia Region

**IR 1.6.1** Increased management capacity in natural resource sector

**IR 1.6.2** Improved policy and regulatory framework

**IR 1.6.3** Sustainable models developed for integrated natural resources management

**IR 1.6.4** Public commitment established for natural resources management policies

### **116-0210 Citizen Participation**

### **116-0211 Strengthened Democratic Culture Among Citizens and Target Institutions**

#### **SO Level Indicator(s):**

Percent of Target Population Exhibiting Civic Consciousness

**IR 2.1.1** Stronger and More Sustainable Civic Organizations

**IR 2.1.2** Increased Availability of information on civic rights and domestic public issues

**IR 2.1.3** Enhanced opportunities for citizen participation in governance

**IR 2.1.4** More Effective, Responsive, and Accountable Local Governance

### **116-0220 Rule of Law**

### **116-0230 More Effective, Responsible, and Accountable Local Governance**

### **116-0240 Conflict Mitigation**

#### **SO Level Indicator(s):**

Percent of Communities Resolved Conflicts

**IR 2.4.1** Strengthened Community Participation

**IR 2.4.2** Improved Local Services Through Community Decisions

### **116-0310 Humanitarian**

### **116-0320 Increased Utilization of Quality Primary Health Care for Select Populations**

#### **SO Level Indicator(s):**

Percent of children less than one year of age completely vaccinated against hepatitis B (HBV)

Percent of total outpatient visits that occurred in PHC practices in pilot cities

Percent Sputum Smear Positive TB Patients cure through DOTS in Pilot Sites

**IR 3.2.1** Select populations are better informed about personal health care rights and responsibilities

**IR 3.2.2** Improved quality of health care including infectious diseases and maternal and child health

**IR 3.2.3** Improved use of health care resources for primary health care

**IR 3.2.4** Improved legislative, regulatory and policy framework

### **116-0330 Environmental Health**

### **116-0340 Improved Quality and Access to Basic Education in Target Areas**

#### **SO Level Indicator(s):**

Attendance Rate Increased

Completion Rate Increased

Percent of Stakeholders Satisfied with Quality of Education in Target Areas

**IR 3.4.1** Improved Quality and Access to In-Service Teacher Education in Target Areas

**IR 3.4.2** Increased Parent and Community Involvement in Target Areas

**IR 3.4.3** Strengthened Institutional, Management, and Technical Capacity in the Education System

**116-041 Special Initiatives**

**116-0420 Cross-Cutting Programs**